GIC Group *An integrated agribusiness consulting and investment advisory firm*

The Changing Structure of Agriculture

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December, 2009

FARM FOUNDATION FORUM

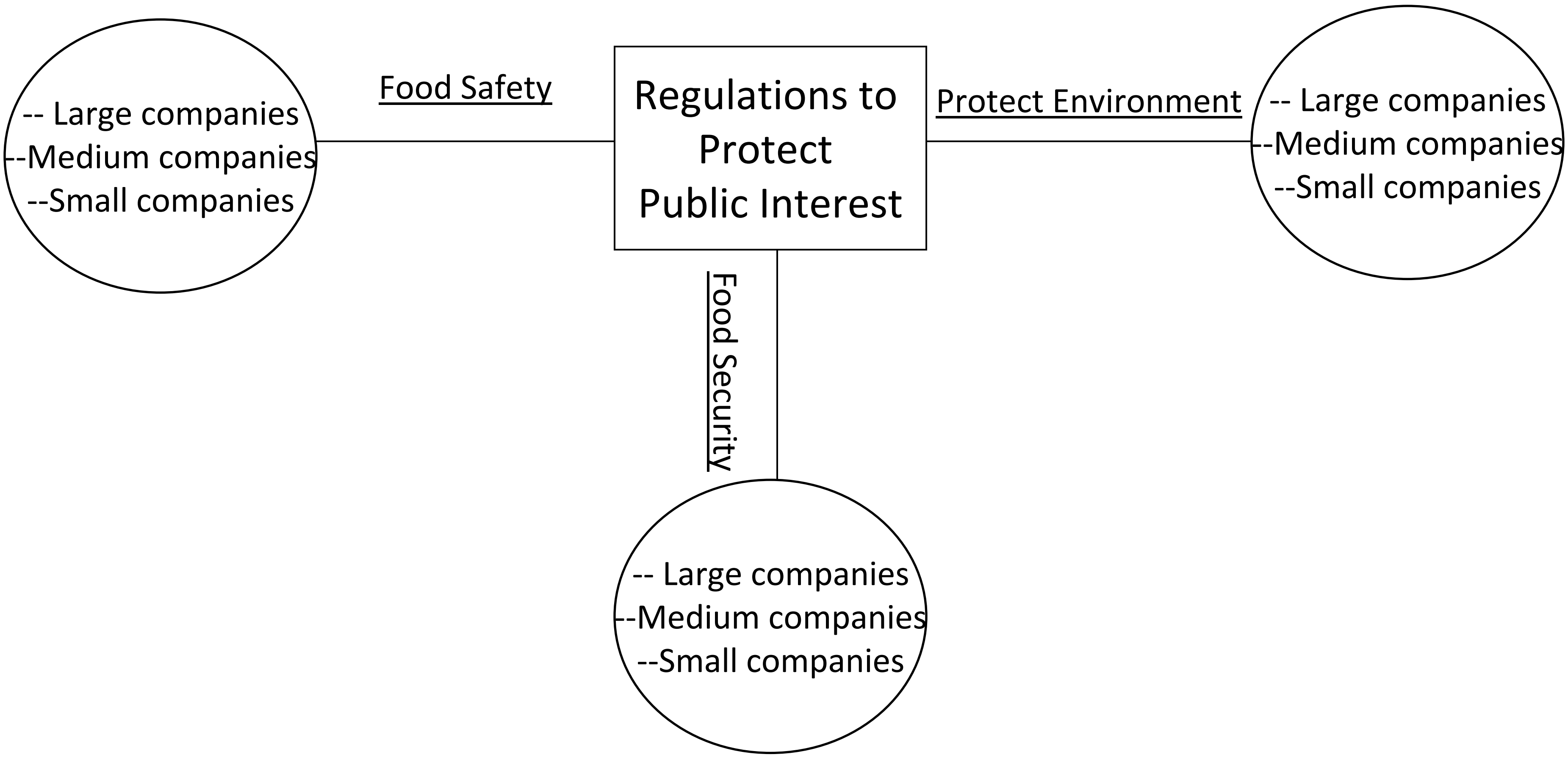
Industry Consolidation Trends in the US

- Increasing capitalization and scaling requirements for production and value-added agriculture for
  - operating costs,
  - R&D,
  - new product launches;
  - global manufacturing and distribution in a diversity of markets
- Integration of markets from farm to fork and to new, industrial end-uses:
  - Regional
  - National
  - International
- Increase in regulation
- Survival rates in global economic recession

Competitiveness and New Technologies

- Infrastructure and Operations
  - Cost-effective operations
  - Inventorying and logistics management
- Market volatilities:
  - Risk minimization strategies
  - Hedging
- Climate change
  - Land
  - Water
  - GHG
- Food safety
  - Product traceability
  - Certification
  - Shipping and handling

Regulation and Consolidation:
New Economic Imperatives



Regulations: Breakdown and Build-Up

- 2008 run-up in wheat prices in wheat futures contract: manipulation by a food cartel?
  - Commodity index traders held between 35% and 50% of all outstanding wheat futures contracts on the Chicago exchange.
  - The average gap between futures and cash prices of wheat at maturity on the Chicago exchange grew from about from 13 cents per bushel in 2005, to $1.53 in 2008.
  - Tentative conclusion was that commodity index traders were one of the engines in the price run-up and subsequent sharp fall due to excessive redemptions forcing hedge funds to cancel out of their short positions.

Regulations: Breakdown and Build-Up, cont'd

- Impact: whose ox was gored?
  - Food industry (They were buying for inventories, not to hedge long or short exposures)
  - Merchandisers
  - Consumers: run-up in prices into 2009 when the economic recession was in full swing
- Food Safety: shared problem and shared solution
  - Incidents: Tainted peanut butter scandal in 2009; China's contaminated pet food in 2007; The Jalapeno Incident in 2006; etc.
  - Response: Industry initiatives and new food safety legislation

Regulation: the Cost Hurdles?

cost to comply with the reporting requirements

Total cost *(million)- estimated*		Number of	Ave. cost per facility	
1st year	2nd year	facilities	1st year	2nd year
$115	$72	10,000	**$11,500**	**$7,200**

Reinvestment of earnings ratios

Food Safety

Environment

Food Security

- **Food safety**—requiring harmonized standards, quality controls, certification/ traceability capabilities, all of which raise manufacturing costs.
  - Industry threat: real threat to brand, loss of market share, liability.
    - Costs: estimates vary but the range is around 30% of total manufacturing cost for HAACP/ ISO/ and private industry standard compliance.

- **Environmental regulations/ compliance with Clean Air Act**
  - Paradox: Regulations to protect consumer, environment but also raises cost ratios and creates higher entry hurdles for start-ups and small to medium size companies
  - EPA mandatory reporting

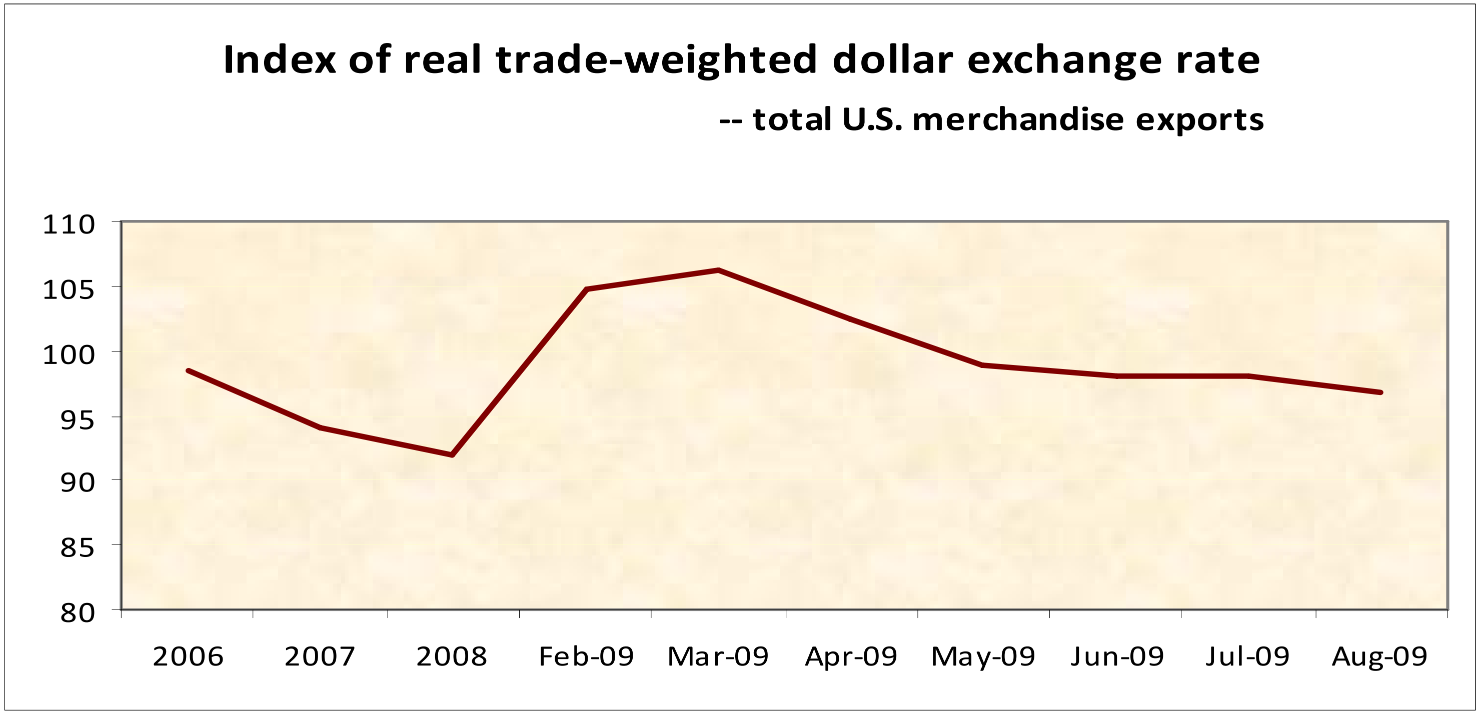
Consumer/End-user Preferences

- Building brand
- Distribution and Convenience
- Supplier services

Financial markets:

New Commercial imperatives

- Exchange rate volatility



- Liquidity
- Transparency

Score Card

- R&D: market entry remains fluid
- Prices
  - Disaggregated pricing more difficult with integrated, international consolidated operations
  - Competitive prices—depends on sector
  - Bias in profit margins in favor of downstream, integrated operations
- Consumer Gains
  - Differentiated product
  - Safer product
  - Reliable supply sourcing
- Producer Gains/Losses
  - *Losses*
    - Lower profit margins
    - Less concentration
    - Fewer risk minimization options
  - *Gains*
    - Greater access to consumers/ end-users
    - Stakeholder participation—i.e., biofuels
    - Additional volumes through new market outlets
    - Opportunities for strategic alliances and cross alliances

Thank You!

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